

MINUTES

**MONTANA SENATE
56th LEGISLATURE - REGULAR SESSION
COMMITTEE ON STATE ADMINISTRATION**

Call to Order: By **CHAIRMAN MACK COLE**, on February 15, 1999 at
11:00 A.M., in Room 331 Capitol.

ROLL CALL

Members Present:

Sen. Mack Cole, Chairman (R)
Sen. Don Hargrove, Vice Chairman (R)
Sen. Jon Tester (D)
Sen. Jack Wells (R)
Sen. Bill Wilson (D)

Members Excused: None.

Members Absent: None.

Staff Present: Keri Burkhardt, Committee Secretary
David Niss, Legislative Branch

Please Note: These are summary minutes. Testimony and
discussion are paraphrased and condensed.

Committee Business Summary:

Hearing(s) & Date(s) Posted: HB 118, HB 119, 2/10/1999
Executive Action: HB 89, HB 118, HB 119, HB 198,
SB 400

HEARING ON HB 118

Sponsor: REP. DOUG MOOD, HD 58, SEELEY LAKE

Proponents: David Senn, Executive Director, Teachers'
Retirement System

Opponents: None.

Opening Statement by Sponsor:**{Tape : 1; Side : A; Approx. Time Counter : 7 - 32}**

REP. DOUG MOOD, HD 58, Seeley Lake, explained he is sponsoring this bill on behalf of the Teachers' Retirement Board. During each interim period there are Federal Statute changes dealing with public retirement systems. It is necessary for the Retirement Board to make sure Montana Statutes align with Federal Statutes. The Retirement Board hired attorneys to make sure the plan would be qualified under the definition of the Internal Revenue Service. It is important they remain qualified, because that is what allows participants to contribute to the plan with tax deferred dollars.

Proponents' Testimony:

David Senn, Executive Director, Teachers' Retirement System, handed out some testimony **EXHIBIT(sts37a01)**. Most of the sections in the bill are bringing the statutes into compliance with what they have been doing through administrative rules and Board policy, in order to make sure they are meeting the qualification requirements of the Federal Government. The 1st handout is a brief overview of the bill. The 2nd handout is an overview of key sections in the Internal Revenue Code. The 3rd handout is a section by section description of **HB 118**. This is a Federal compliance and housekeeping bill. There are a few issues that have been corrected or made clearer because of court decisions or questions their members have.

This bill is necessary for the Teachers' Retirement System to retain its qualified status. The members can then contribute with tax deferred dollars. The investment earnings of the plan remain tax deferred until the members receive retirement benefits. If income taxes had to be paid on the investment income received, they would need a much higher contribution rate in order to remain actuarially sound. It allows them to transfer the member's account to another public retirement plan if they choose to move out of state. This allows them to accept plans or assets from another qualified plan from someone moving into Montana.

Section 1 is amending the provisions related to legislators who are members of a public retirement plan. They can elect to participate in the public retirement plan while they are serving in the Montana legislature so they don't have any loss in service. They are amending the current provisions to comply with the Internal Revenue Code. The individual has to make an irrevocable election within 6 months following their election or

6 months following the effective date of this bill, for those legislators that are currently teachers and want to continue to participate in the Teachers' Retirement System. He will notify every legislator that they are allowed to participate in Public Retirement System. If the legislator is already part of a Public Retirement System, he will be notified he can continue participating in the Retirement System without losing any credit. They have put in a new definition for "retired member". Termination of employment is required before the person is eligible to receive retirement benefits.

Section 4 is the General Internal Revenue Service qualification rules. It didn't fit into the current statutes in the Teachers Retirement system. They put in a general area to reference those sections into a Revenue Code they must comply with. When the Internal Revenue Service looks at a plan to see if it qualifies, they look to see if proper references have been cited in the plan document. For a state agency, the plan document is the state law. This section also provides for the Board to maintain an excess benefit arrangement under Section 415 of the Internal Revenue Code, which is an area that limits the amount of benefits. The Internal Revenue Code allows the agency to establish an excess benefit arrangement, which allows them to pay the benefit the legislature and the State of Montana has promised to a member and not violate any of the federal requirements.

Section 9 deals with purchase of service credit and pick up. An employer pick up is an individual making the election to have the employer reduce their salary for purchasing service credit. This is an advantage to their members because it helps them avoid some of the 415 limits imposed. A member could not purchase more service if it allows their benefit to go past \$130,000 a year. In order for the pick up procedure to work for purchasing additional service, the enabling legislation has to be passed by the Montana Legislature. They must get a favorable letter ruling from the IRS, which they have requested. It has been verbally approved. They are going to require each employer to adopt a resolution saying they want to make this available to their employees. Employers are going to have to make some changes to their accounting and payroll systems so they need time to get this in place. Each employee will have to sign an irrevocable election. The only way out of an irrevocable election is to terminate the employment or die. Once an individual signs up, they have a payroll deduction for the term they have elected.

Section 10 deals with credit for legislative service required. If the legislator does not sign that irrevocable election to participate in the Teachers' Retirement System in which they are already a member, they can come back at a later time and purchase it, but they will then be subject to the 415 limitations. They

will have to pay interest on the contributions that were not made. The employer contributions paid for legislative services are paid by the Legislative Services Division. He doesn't see this increasing the cost in the contributions paid by the Legislative Services Division. Most legislators who are members of the Teachers' Retirement System wait until they are about ready to retire and then want to purchase the time served in the legislature. The Legislative Services Division pays all the back contribution in a lump sum. Therefore, this may have the impact of reducing that a little bit.

Section 17 addresses the maximum benefit limitation. The \$130,000 limitation is found in 415 B of the Internal Revenue Code. There is another limitation in 415 C of the Internal Revenue Code. This is more problematic for teachers because they have an option to contribute on termination pay, a lump sum payment of sick or annual leave at the time of termination. The IRS limits those kinds of contributions to 25% percent of the members salary. They are contributing termination pay at the time of termination. If the Teachers' Retirement System has not had any contributions through a member's career, it is a lump sum at the time of termination. That contribution is very high as it is the actuarial cost. One way to avoid the limitation of 25% percent of salary for an individual is to allow it to be deducted under the employer pick up. Then the only limit they have to worry about is the \$130,000 limitation in 415 B. Without the change in termination pay, they would be reducing benefits for members because members would not be able to contribute on all of their termination pay. By being picked up and paid by the employer and signing an irrevocable election at least 90 days prior to termination, they can solve the problem with 25% percent limit. There could be potential problems for individuals who decide at the last minute they are going to retire. They may or may not run into a limit. The 90 day irrevocable election is not a resignation. They will have to work closely with teachers concerning the deductions for tax deferrable annuities because all of these IRS limitations come together. They have been traveling across the state talking to teachers about this legislation.

Section 19 deals with maximum contribution limitations. These need to be cited in the Teachers' Retirement Act, but with everything else they have done in the bill he does not see a problem for the members of the system. Section 23, a housekeeping amendment, clarifies the duties and responsibilities for the Board's representative when reviewing disability applications. There are times when they receive a disability application that clearly shows the applicant is disabled. They would like to start payment as soon as they terminate employment, but they can't because the Board doesn't meet for a couple of

months. The Board meets 4 to 5 times a year. Teachers often do not apply until the end of the school year. This amendment would give the staff the option to start that benefit as soon as possible, rather than waiting for a September Retirement Board meeting. The final disability would still be approved by the retirement board. If it was denied by the board, they would go back and adjust the benefit to a regular retiree benefit. For the majority of disabilities, the regular retirement benefits are the same dollar amount. The only advantage to applying for the disability benefits are some tax advantages. The other advantage with the disability benefit is a minimum benefit based on 15 years of service. They could receive a greater benefit if they have less than 15 years. The majority of the disability applicants have more than 15 years in the Teachers' Retirement System.

The repealer sections are repealing a provision that allows members to buy 1 additional year for each 5 years that they have served, if they have membership in the Teachers' Retirement System. This provision is problematic with the IRS. No one purchases this type of service because it is the most expensive service they can buy. They have a saving clause in Section 28 to protect anyone who is currently purchasing that service or has purchased it. They are repealing 19-24-13, which deals with the purchase of salary credit. This was put in the Teachers' Retirement System as a way to help people purchase salary if they missed salary while on strike. When the actuarial cost is charged at the time of retirement for a benefit, it is very expensive and no one wants to purchase it. No one has ever purchased it. They are repealing the ADHOC cost of living adjustments the legislature passed that should have been temporary provisions in the Teachers' Retirement Act.

{Tape : 1; Side : A; Approx. Time Counter : 32 - 41}

Don Waldron, Montana Rural Education Association, said they feel comfortable the Teachers' Retirement has their best interests in mind.

Eric Feaver, Montana Education Association, supports this bill.

Questions from Committee Members and Responses:

SEN. HARGROVE asked **Mr. Senn** to explain the difference between salary credit and years of service. **Mr. Senn** said the salary credit is a calculation of the member's average final salary by averaging the member's three highest consecutive years' salaries. Service credit is 1 year service credit for each school year.

SEN. HARGROVE asked what is bought if a salary credit is

purchased. **Mr. Senn** responded they can purchase the salary of their daily rate for time on strike. They pay a formula of 5.7% percent per year of service multiplied by that salary. They pay more than a 100% percent of the salary they lost as the actuarial cost. **SEN. HARGROVE** asked if a person who is a teacher and a legislator was paid for both during the legislature. **Mr. Senn** explained most school districts in the University do not pay teachers who are in the legislature during that legislative service time, but some may pay a partial payment during the legislative service time. **SEN. HARGROVE** asked what the contribution would be for a teacher in the legislature and where it comes from. **Mr. Senn** said under current law, the teacher has an option to contribute on the salary rate of a legislator or the daily salary of a teacher. The salary rate of a legislator is typically lower than that of a teacher. Therefore they typically opt to contribute on their legislative salary, except in the final 3 years when it matters in calculating the final average salary. This is a problem in complying with the IRS regulation of giving people options to select against the system. This bill says those currently in the legislature must make that election within 6 months after taking office or the effective date of this bill. They would contribute on their salary as a member of the Teachers' Retirement System.

SEN. TESTER asked **Mr. Senn** to clarify current portability of people coming in and out of the system and how this bill changes that. **Mr. Senn** said they currently accept contributions from another retirement plan and they do transfer contributions. This bill clarifies the statute the way the IRS would like to see it written. They are not stated specifically under the current law. **SEN. TESTER** asked if this is just a clarification of the law, but won't cause any change. **Mr. Senn** responded he was correct.

SEN. COLE said this bill clears up any contradictions between the IRS and the retirement. The other portion dealt with legislators who are involved with Teachers' Retirement. **Mr. Senn** said he was correct and it also relates to the Internal Revenue Code provision. **SEN. COLE** said the Fiscal Note states this would not have any effect. **Mr. Senn** stated he was correct.

Closing by Sponsor:

REP. MOOD closed.

HEARING ON HB 119

Sponsor: **REP. DOUG MOOD, HD 58, SEELEY LAKE**

Proponents: **Mike O'Connor, Executive Director, Public
Employees Retirement System
Don Waldron, Montana Rural Education Association**

Opponents: None.

Opening Statement by Sponsor:

REP. DOUG MOOD, HD 58, Seeley Lake, sponsored this bill on behalf of the Public Employee Retirement Board. He explained this bill is to ensure they remain qualified as a plan for the benefit of the members.

Proponents' Testimony:

{Tape : 1; Side : A; Approx. Time Counter : 41 - 49}

Mike O'Connor, Executive Director, Public Employees Retirement System, explained they hired an outside tax counsel to review all the statutes of the retirement systems to make sure they comply with IRS. This bill incorporates the changes needing to be addressed in the statutes **EXHIBIT(sts37a02)**. They are attempting to fine tune the retirement statutes to make sure they maintain qualified plan status. When they are done with this, they are going to submit their plan document and **HB 119** to the IRS for a private letter of ruling to make sure their plans meet the qualification requirements of the IRS. They are also trying to take advantage of the favorable tax treatments available through the IRS. Many of the sections are similar to **HB 118**.

The first 3 sections of the bill address the Social Security chapter. The Social Security Administration assessed a 39 million dollar bill. The Public Employees Retirement System gathered all the information from local government and got the 39 million down to 2.1 million. They collected contributions and interest from all state and local governments for the 2.1 million. They did have to pay the contributions for that time period, but they reduced the interest charge 70 percent. When they settle this, they will pay the Social Security contributions and 30 percent of the interest and refund 70 percent of the interest to state and local governments.

The first 3 sections say the administration of the Social Security part go to the Department of Administration for storage of the records. It will cost \$140 per year to store those records. The Public Employees Retirement System has paid the bill to settle this agreement, so they want to reimburse PERS for cost of the settlement.

{Tape : 1; Side : B; Approx. Time Counter : 49 - 69}

Section 6 deals with members receiving refunds and specifies when a refund can happen. The IRS allows public and private plans to refund contributions of \$200 or less without an application. Section 6 allows the refund if it is a dormant account. People who have balances of \$200 to \$5,000 can be refunded if they are non-vested. This gives them a pro-active approach so they do not increase the number of dormant accounts.

Title 19, Chapter 2, addresses all the retirement systems they administer. They have a separate chapter for each retirement system they administer for specific things pertaining only to individual retirements systems. Chapter 2 addresses all retirement systems and takes advantage of favorable tax treatments from the IRS. The employer pick up is found here. Members can purchase service with pre-tax money if they file an irrevocable election. They have people who purchase service years, therefore they do not want to eliminate it. They want their members to be able to purchase with pre-tax money in order to eliminate the 415 limits. They are cleaning up the other retirement statutes and putting all the information relating to service purchases in Chapter 2. They addressed the military service purchase. In order for retirement plans to comply with the IRS, they must comply with USERRA. There are some sections of military service that are more restrictive than Federal law allows. They are striking the restrictive sections and making sure each section addressing military services complies with Federal law.

Section 10 deals with the ability of members to roll over into the system and be able to purchase service. The IRS also sets limits on how much a retirement plan can pay out. Sections 12, 13, and 16 address what they can pay out and when they can pay out benefits. There are required distributions the IRS is looking for. The outside tax council had an issue with optional service. There are groups of people who have the option of joining PERS. The IRS has a problem giving a person the option of electing into PERS at any time during their career and it doesn't meet the qualification rules. They are going to allow people to opt into the system, but they must make an election within 6 months of their hire date. This does not prevent them from purchasing service at a later date.

Section 43 eliminates language allowing mental health corporations to join the system. Mental health corporations are non-governmental and the statute does not allow non-governmental agencies to be a member of the system. They currently have one mental health corporation. The members currently in the system will continue to be in the system, but any new hires would not be

able to be members of the system. They are repealing the section on public administrators, so public administrators are treated like any other government employee.

Don Waldron, Montana Rural Education Association, is in support of this bill. He said they will work to get the new information out to their employees.

Questions from Committee Members and Responses:

SEN. TESTER asked **Mr. O'Connor** if it is in the law that PERS can exempt other privatizations in government. **Mr. O'Connor** said several years ago there was a move to privatize county hospitals. Once they are privatized, the members who are employees of that hospital have an option to retire or roll over into another system. When this happens, they work with the individual agencies to inform people of their options and what is available to them. Once they are privatized, they are not able to be members of PERS. **SEN. TESTER** asked him to clarify the statute regarding mental health corporations. **Mr. O'Connor** said that the statute allowed them to be members of PERS and they are striking that statute. **SEN. TESTER** said this is specific to mental health corporations and asked if **Mr. O'Connor** has the ability to not allow people in government agencies that become privatized to be a part of PERS, as long as they are new hires and are not vested. **Mr. O'Connor** said that was correct.

SEN. HARGROVE asked what is a qualified plan and who determines whether it can be rolled over into PERS. **Mr. O'Connor** said the IRS determines what a qualified plan is and who can roll over into it. They have regulations saying any qualified plan can roll over into another qualified plan. **SEN. HARGROVE** asked if there was a definition of a qualified plan. **Mr. O'Connor** said they will be applying to the IRS for a letter of determination. If someone wanted to roll over into the system, they would ask for the qualification letter from IRS. **SEN. HARGROVE** asked what a public administrator is. **Mr. O'Connor** explained a public administrator is an individual who takes care of indigent people who have died, including their records, their burial, and locating their relatives.

SEN. COLE asked if taking retirement at 70 1/2 years of age is a federal law or a state law. **Mr. O'Connor** stated it was a federal rule and added it applies to government and private plans.

Closing by Sponsor:

REP. MOOD closed.

{Tape : 1; Side : B; Approx. Time Counter : 69 - 81}

EXECUTIVE ACTION ON HB 118

Motion/Vote: SEN. WELLS moved that HB 118 BE CONCURRED IN.
Motion carried 5-0.

EXECUTIVE ACTION ON HB 119

Motion/Vote: SEN. TESTER moved that HB 119 BE CONCURRED IN.
Motion carried 5-0.

EXECUTIVE ACTION ON SB 400

Motion/Vote: SEN. WELLS moved that SB 400 BE REMOVED FROM THE
TABLE. Motion carried 4-1 with SEN. WILSON voting no.

Motion: SEN. WELLS moved that SB 400 DO PASS.

SEN. WELLS explained he would like to discuss it on the Floor of the Senate. He understands the objections from the school boards. However, he thinks there are a lot of advantages to this change.

SEN. HARGROVE stated he would vote to have it passed, but would like for someone to bring up the concerns about the school busses.

Vote: Motion carried 4-1 with SEN. WILSON voting no.

EXECUTIVE ACTION ON HB 198

Motion/Vote: SEN. WELLS moved that HB 198 BE CONCURRED IN.
Motion carried 5-0.

EXECUTIVE ACTION ON HB 89

Motion/Vote: SEN. TESTER moved that HB 89 BE CONCURRED IN.
Motion carried 5-0.

ADJOURNMENT

Adjournment: 12:21 A.M.

SEN. MACK COLE, Chairman

KERI BURKHARDT, Secretary

MC/KB

EXHIBIT (sts37aad)